

No. 2685

IN THE
United States Circuit Court of Appeals

For the Ninth Circuit

W. L. WILSON, EMIL E. LENGUETIN, FRED
F. CONNOR, JOHN A. BLOOM, LAWRENCE
HOBRECHT and BENJ. F. CURRIER,
Petitioners,

vs.

THE CONTINENTAL BUILDING AND LOAN ASSO-
CIATION (a corporation) et al.,
Respondents,

In the Matter of
CONTINENTAL BUILDING AND LOAN ASSOCIA-
TION (a corporation),
Bankrupt.

BRIEF ON BEHALF OF PETITIONERS.

B. M. AIKINS,
Attorney for Petitioners.

Filed this.....day of March, 1916.

FRANK D. MONCKTON, *Clerk.*

By.....Deputy Clerk.

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Statement of Case.

Some time prior to August 9, 1915, The Continental Building and Loan Association filed a voluntary petition in bankruptcy with a schedule in which it named its stockholders as creditors. On August 9, 1915, it was adjudged a bankrupt, and all further proceedings were referred to Armand B.

Kreft, Esquire, Referee in Bankruptcy. The first meeting of creditors was held on August 30, 1915. At that meeting a large number of these stockholder-creditors appeared, and elected one B. G. Tognazzi their trustee. The Referee disapproved the election because he had had the active support of the directors of the bankrupt, and continued the meeting until September 15, 1915, when a new election was held and the Anglo-California Trust Company was elected. The other candidates were W. R. Williams, State Superintendent of Banks, and the Union Trust Company. The Anglo-California Trust Company had the support of four hundred three (403) claimants, whose claims aggregated about three hundred twenty thousand four hundred thirty-seven and 50/100 dollars (\$320,437.50); Williams had two hundred and two (202) claims aggregating about one hundred forty thousand dollars (\$140,000.00); and the Union Trust Company, one hundred and seven (107) claims aggregating about sixty-two thousand dollars (\$62,000.00). (Record p. 23.)

The only claimants who voted were the stockholders of the bankrupt corporation, who acquired the status of creditors, or quasi-creditors, by virtue of the bankruptcy proceedings and of the right to share in the proceeds of liquidation in proportion to their various payments upon their several stock subscriptions, most of the stock being payable in small, monthly installments.

Counsel representing the claimants who voted for Williams and the Union Trust Company thereupon objected to the election of the Anglo-California Trust Company on two grounds:

First: That said company was the depositary of the bankrupt and had acted as trustee on its deeds of trust;

Second: That its election was brought about by activity on the part of the officers, directors and attorneys of the bankrupt (p. 23).

Upon these issues evidence was introduced, and thereafter the referee sustained the objection and for the second time disapproved the election of the majority candidate.

On September 27, 1915, the petitioners presented a petition for a review of the referee's order by the District Court (pp. 17-19). On October 2, 1915, the referee filed his certificate on petition to review (pp. 20-47). A hearing on the petition was had before the Hon. M. T. Dooling, D. J., who denied it on November 9, 1915. It is this order which your petitioners now seek to review.

The order is based squarely upon the ground that the selection of that company as trustee was

“influenced, if not brought about by the officers of the bankrupt, and the attorneys of the bankrupt”,

and ignores the contention that the Anglo-California Trust Company was disqualified by having been the depositary of the deeds of trust of the bankrupt

or by having been named as trustee in deeds of trust securing its loans.

Assignment of Errors.

The following are the formal assignments of error contained in the record (pp. 17-19) on which petitioners rely:

“First. That the Anglo-California Trust Company was elected by a great majority of the creditors present or represented at said meeting, both in number of creditors and in the amount of their claim, but was without adequate cause disapproved.

“Second. That the Anglo-California Trust Company is not disqualified to act as a trustee by reason of its having acted as the depository of the securities of the bankrupt, if true; and that no proof was offered or made of such alleged fact, and the fact was not so found.

“Third. That said Trust Company is not disqualified to act as trustee by reason of its having acted as trustee under deeds of trust for the bankrupt, if true; and that no proof was offered of such alleged fact, and the fact was not so found.

“Fourth. That said Trust Company is not disqualified by reason of the necessity of the trustee herein to examine into the relation existing between the said company and the bankrupt, if true; and that no proof was offered of such alleged necessity, and the fact was not so found.

“Fifth. That the said Trust Company is not disqualified by reason of the counsel of the bankrupt being an attorney of the said company, even though true; and that no proof

was offered or made of such fact, and that the fact was not so found and that such is not the fact.

“Sixth. That it is not true that the election of the said Trust Company was produced or brought about by activity on the part of the officers, directors and attorneys of the bankrupt.

“Seventh. That there was no evidence before the referee to show any activity on the part of the officers, directors and attorneys of the bankrupt, or any of them, to produce or bring about the election of said Trust Company.

“Eighth. That there was no evidence before the referee to show that any activity on the part of the officers, directors and attorneys, of the bankrupt, or any of them did in fact influence any of the creditors to vote for said Trust Company as such trustee.

“Ninth. That there was no evidence before the referee to show that such alleged activity did influence the votes of a sufficient number of creditors, if any, to change the result of the election.

“Tenth. That the evidence wholly fails to show that the persons whose alleged activity was deemed obnoxious by the referee were not all stockholders, with the same qualified status of creditors as those who opposed its election.

“Eleventh. That the decision of the referee in effect disfranchises the said officers and attorneys.

“Twelfth. That the said decision complained of in effect disfranchises the majority of the creditors for the benefit of the minority.

“Thirteenth. That the decision complained of constitutes an abuse of discretion on the part of the referee.”

Brief of Argument.

Some apology is due to the court for the inability of petitioners to present the issues in as clear cut a manner as is desirable. Our excuse must be the very unusual practice followed in this case, which merits a word of explanation.

The unusual nature of the practice followed consisted in:

(1) The failure of the referee to make any finding of fact and to clearly certify the precise question for review;

(2) In including in his certificate an extended argument in support of his decision; and

(3) In admitting evidence outside of a creditors' meeting and after the original hearing had been terminated, after his order of disapproval had been made and after the petition to review had been actually prepared and filed.

1. The rules require a finding as well as an order.

"When a bankrupt, creditor, trustee, or other person shall desire a review by the judge of any order made by the referee, he shall file with the referee his petition therefor, setting out the error complained of; and the referee shall forthwith certify to the judge the question presented, a summary of the evidence relating thereto, and the finding and order of the referee thereon."

General Orders in Bankruptcy, XXVII.

They also require a clear and distinct statement of the precise question for review.

“The referee is also distinctly and clearly to state and certify the precise question for review; *for the hearing will be confined to the questions involved in the issue tried.*”*

Remington, Sec. 2858.

As before observed, no finding has been certified, and none was made, and in the absence of findings and of an exact statement of the question for review, it is only too evident that petitioners' task is not an easy one.

2. The certificate contains an extended argument with the citation of authorities and the discussion of rules which not only increases the burden of petitioners in securing a record, but further complicates the presentation of their arguments by reason of the obvious necessity of not permitting any of the referee's arguments to go unanswered, since they carry a force that they would not have coming from counsel. Hence they put us in the position of having to reply in an opening brief.

It is respectfully submitted that arguments have no place in such a document, which has been likened to a bill of exceptions.

Remington, Secs. 2857, 2858.

3. We are also somewhat embarrassed by the fact that the referee permitted the case to be reopened after the petition for review had been filed, for the reception of further evidence upon certain issues which, happily, do not seem to be of great importance.

* Italics ours throughout.

Following the presentation of our petition, the writer received a notice (of not more than an hour or two) from counsel for certain creditors who had objected to the Anglo-California Trust Company, that certain additional evidence would be introduced.*

The writer appeared at the referee's office at the time indicated in the notice, as did counsel giving the notice, and found there Mr. Grant Cordray, trust officer of the Anglo-California Trust Company, who had been subpoenaed to testify before the referee, and after an informal discussion of the facts with Mr. Cordray, the stipulation referred to by the referee (p. 34) was entered into, at the request of counsel for respondents, *but subject to the objection that the issues having been made up*

* The notice was in letter form, as follows:

"Wednesday, September 29th, 1915.

"B. M. Aikins, Esq.,
"Attorney at Law,
"Mills Building,
"San Francisco.

"In re Continental Building & Loan Association.

"Dear Sir:—

"I address you this communication because you appear in this matter as attorney for the creditors who are seeking to review the order of Referee Kreft disapproving the election of the Anglo California Trust Company as trustee.

"Please be notified that at 2 o'clock P. M. this afternoon I will introduce before the referee in bankruptcy evidence upon the following points:

"(1). That Gavin McNab is a director of the Anglo California Trust Company;

"(2). That Gavin McNab is the attorney for the Anglo California Trust Company;

"(3). That the Anglo California Trust Company holds the securities of the bankrupt;

"(4). That the Anglo California Trust Company is the trustee upon a large number of trust deeds now outstanding in which the bankrupt is the beneficiary;

"(5). That the Anglo California Trust Company receives deposits from the bankrupt.

"Yours very truly,

"Reuben G. Hunt."

and the petition for review filed, no further evidence could be taken.

These circumstances and the nature of the petitioners' objection to the evidence covered by the stipulation do not appear in the referee's certificate, but he explains the admission of the evidence after the closing of the case and the filing of the petition for a review, as follows:

"On offering testimony in support of his objection Mr. Hunt stated that he desired to show that Mr. McNab is a director of Anglo-California Trust Company, and that said company has acted as trustee for the Continental Building & Loan Association, but he needed a continuance to call witnesses for this purpose. I stated that if it became necessary to certify the matter to the Court I would permit him to complete this record in this respect. Being satisfied from the evidence already presented that Mr. Hunt's objection should be sustained, I concluded to decide the matter on the record as it then stood."

The referee, as intimated, overruled the objection and admitted the evidence contained in the stipulation.

This explanation is made, as above intimated, to excuse what may seem to the court a want of precision in presenting the points which are in issue, and not in any sense as a criticism of the referee.

The referee has no discretion to disapprove the election of a trustee who is elected by a majority of creditors, both in number and amount, on account of the activity in his behalf of certain of the officers, directors, employees and other stockholders, where the only other creditors of the bankrupt are such, like themselves, in a secondary sense only, and this solely by reason of being stockholders or distributees.

1. AS TO THE RIGHT IN GENERAL OF CREDITORS TO SELECT THE TRUSTEE.

It will not be disputed that the majority of the creditors, in number and amount, have the right to select the trustee.

This right is created by the Bankrupt Act itself:

“The creditors of a bankrupt estate shall”
* * * appoint one trustee or three trustees of such estate.”

30 Stat. L. 557, Sec. 44.

and carries special weight by reason of its statutory origin.

“The statute gives to the creditors the right to elect a trustee. The selection of a trustee by the creditors ought not to be lightly set aside. He should be confirmed unless there is good reason to believe that the election was controlled in the interest of the bankrupt or by some influence opposed to the interests of the creditors, so as to imperil the fair and efficient administration of the estate.”

Loveland, p. 589.

2. AS TO THE RIGHT OF THE REFEREE TO DISAPPROVE.

The written authority for this right is found in Gen. Order No. XIII:

“The appointment of a trustee by the creditors shall be subject to be approved or disapproved by the referee or by the judge and he shall be removable by the judge only.”

This right is not arbitrary and can be exercised only for cause.

In re Kreuger, 196 Fed. 705;

In re Lazoris, 120 Fed. 716.

“It is to be remembered in all such cases that the choice of a trustee is lodged by the law with the creditors constituting a majority in number and amount, and that their selection is not to be interfered with, unless it clearly imperils the fair and efficient administration of the estate. I am not persuaded that there is any such danger in the present instance, and, if it should prove otherwise, the objecting creditors have their remedy by an application hereafter to remove.”

In re Blue Ridge Packing Co., 125 Fed. 622;

In re Syracuse Paper & Pulp Co., 164 Fed. 280.

Elsewhere it was held, after an extensive discussion of the authorities, that

“they establish the rule that the election of a trustee by the creditors is not to be disapproved, unless there is good reason for believing that the election has been directed, managed, or controlled by the bankrupt or his attorney or by some influence opposed to the creditors’ interests.”

In re Eastlack, 145 Fed. 73.

The usual ground of disapproval is that the election of trustee was in fact brought about by the activity of the bankrupt or those in collusion with the bankrupt. Such was the fact in all of the cases cited by the referee in his certificate. Indeed we have found no case based upon any other ground.

It may be conceded, however, that this is not necessarily the only ground. It is conceivable that the trustee might be incompetent or inherently so unsuitable as to endanger the safety of the administration. But the showing would have to be a very strong one to warrant the disapproval of the trustee where there was no question of his being the real choice of the creditors, or, as said in *In re Henschel*, 111 Fed. 443.

“the emergency should not be a trivial one; it should be one of grave character and due weight.”

In this case objection was made to the Anglo-California Trust Company on two grounds, and on two grounds only:

Because its election was brought about by the activity of the bankrupt's officers, and because it had acted as trustee under and depository of the deeds of trust securing the investments of the bankrupt. There was no question of any grave emergency threatening the safety of the administration of the trust by the Anglo-California Trust Company.

3. AS TO THE PECULIAR STATUS OF THE CREDITORS HERE.

Before proceeding further with the argument, a statement should be made upon this point.

The situation is a very unusual one, as will immediately appear from the consideration that there are no true creditors to be taken into consideration, the only persons having the true status of creditors being so abundantly assured of the full payment of their claims as to exclude them from any part in the administration of the bankrupt estate.

The status, therefore, of every creditor who is entitled to participate in the election is more accurately that of a distributee entitled to participate in the proceeds of liquidation after the payment of the true creditors. As stated by the referee in his argument, they are corporate co-partners rather than technical creditors (p. 40), citing *Towle v. American Building Loan and Investment Co.*, 61 Fed. 466 (Grosscup, D. J.), which, it may be noted in passing, was a suit in equity involving a liquidation, not a bankruptcy proceeding.

The learned District Judge below seems to have entertained some doubt as to the right of anyone to vote at the election of trustee, the only true creditors being eliminated by the richness of the bankrupt's estate, but concluded that the question whether stockholders can be at the same time creditors was unnecessary of determination, since:

“No one interested has made any objection to the adjudication and so long as it stands, based on the theory that the stockholders are

creditors, they must be regarded as creditors for all purposes" (p. 48).

Their status, therefore, is fixed by acquiescence. They are creditors by estoppel.

But upon whatever theory they are to be deemed as creditors and entitled to vote for a trustee, it is most important to keep in mind *that they are all creditors because they are stockholders, that they all occupy the same status, and that "they must be regarded as creditors for all purposes."*

4. THE RULE AGAINST PERMITTING THE BANKRUPT TO CONTROL THE ELECTION OF TRUSTEE CAN APPLY IN THE NATURE OF THINGS ONLY WHEN THE CREDITORS AND THE BANKRUPT ARE NOT IDENTICAL.

The referee insists in his certificate (p. 36) that the courts have uniformly refused to approve of trustees chosen through the influence of officers of, or attorneys for the bankrupts. In support of this proposition he cites many cases (pp. 36-37). These cases have all been examined and in every one of them there were true creditors whose interests were distinct from those of the various bankrupts, the creditors not being identical, as here, with the bankrupt.

The doctrine they teach is that the creditors, and they alone, have the right to select the trustee, and that if the election is not in fact that of the creditors, but is brought about in the interest of the bank-

rupt, by its officers, attorneys, or stockholders, the referee may disapprove.

The foundation of the creditors' right of selection is, as we have already seen, the statute. And the rule that the trustee must not be selected through the influence of the bankrupt, its officers, attorneys, or stockholders, is merely a negative outgrowth of the statute limiting the right of selection to the creditors. It is, therefore, a rule in aid of the statute, designed to give effect to it, not to defeat it.

In applying this rule the courts have repeatedly drawn attention to the necessity of protecting the creditors against the bankrupt, and have refused to approve elections accomplished in the interest of the bankrupt by the activities of its officers, directors, employees or stockholders.

The reason of the rule is therefore to assure to the creditors their statutory right of selection in order to protect them against the bankrupt.

In this case, however, it must be evident that no such reason can exist. The creditors are all stockholders and are creditors solely by reason of being stockholders and are all "entitled", as stated by the referee, "to their proportionate share of the profits, if any" (p. 42). How then can there be room here for any distinction between creditor and bankrupt? An election accomplished in the interest of the bankrupt as against that of the creditors is an obvious absurdity where creditors and the stockholders are identical.

Moreover, the application of the rule in this case is not possible. For the cases make no distinction between the activities of officers, directors, attorneys or stockholders (Remington, Sec. 888), the forbidden thing being the activity of any of these persons in the interest of the bankrupt and against the interest of the creditors. The rule must therefore be applied, if at all, against stockholders as well as those connected with the management of the corporation. But all of the respondents in this case (except The Merchants National Bank) are stockholders, and the contest for trustee was simply a contest between three groups of stockholders, and it is clear that no such spirited contest could take place among so many creditors without the existence of activity in each of these groups. Such an election cannot be conducted by silent prayer. Co-operation is necessary. And if none of the stockholders may suggest and canvass the trustee of his choice it is clear that there never can be any election at all, since all are stockholders. Yet in this case the largest group of electors, representing a clear majority over both of the others, both in number and amount, is denied its choice of trustee because among its numbers are found certain stockholders who were directors and officers of the "corporate copartnership" and who advocated the election of the same trustee. They were the "agents" of every stockholder (p. 40) and had been chosen for many years by the majority of the stockholders (p. 45), (treated here as credit-

ors by a species of estoppel) as their trusted agents to manage their affairs. And this very expression and proof of confidence on the part of those who are entitled to select the trustee is, by the false, and be it noted the *partial*, application of a rule which was not devised and never could have been devised, for such a case, made the instrument of defeating the purpose of the statute, to wit, the will of the majority. To apply the rule *to all* of the stockholders in each of the three groups, as it should be applied, if at all, would be impossible because in such a case no trustee could ever be selected free from the taint of activity of stockholders.

Again. Respondents' contention, if sound, would bring us to this: that those particular stockholder-creditors who were officers and attorneys for the bankrupt may, by advocating the candidacy of any nominee, not only defeat him, but deny to the majority of the creditors who participate in his choice their statutory right to elect him.

That the decision complained of is a much strained application of a rule, the sole purpose of which is to protect the rights of the creditors as against the stockholders, must necessarily appear, also, not only from the fact that (1) such a rule could never have arisen unless the bankrupt and the creditors were different persons with divergent interests, and also from the fact (2) that the persons who were denied the right of participating in the campaign for trustee occupy the same status as all others interested and "must", therefore, in the

language of the learned District Judge, "be regarded as creditors for all purposes"; but from the further consideration (3) that the true creditors of the bankrupt being disregarded, this proceeding amounts in effect to a liquidation for the benefit of the stockholders and not to a true bankruptcy proceeding, the objects and purposes of which are twofold:

"First, to secure possession of an insolvent's assets and procure their equitable division among creditors, preventing and avoiding attempts of one creditor to obtain advantage over other creditors therein; and second, to free the worthy debtor from the burden of unpaid debts" (Remington, Sec. 17);

and that the people of this state have repeatedly determined that the proper persons to liquidate the affairs of a corporation are the very persons who were here denied the rights of every other person occupying the same status.

"§ 400. CORPORATIONS, DIRECTORS, TRUSTEES OF CREDITORS, WHEN DISSOLVED, EXCEPT. Unless other persons are appointed by the court, the directors or managers of the affairs of a corporation at the time of its dissolution are trustees of the creditors and stockholders or members of the corporation dissolved, and have full power to settle the affairs of the corporation."

Civil Code, Sec. 400;

Stats. 1850, Sec. 16 (p. 349).

So also, where a corporate charter is forfeited for non-payment of license tax.

“In all cases of forfeiture under the provisions of this act, the directors or managers in office of the affairs of any domestic corporation, whose charter may be so forfeited, or of any foreign corporation whose right to do business in this state may be so forfeited, are deemed to be trustees of the corporation and stockholders or members of the corporation whose power or right to do business is forfeited and have full power to settle the affairs of the corporation” etc.

Stat. 1915, Sec. 13, p. 427;

or for non-payment of franchise tax.

Stat. 1913, Sec. 24, p. 7;

Stat. 1913, Sec. 24a, p. 625.

Under these statutes it has been held that it is only where the directors or other officers have been guilty of fraud that the courts have the right to appoint a receiver.

Havemeyer v. Supreme Court, 84 Cal. 327;

Clark & Marshall on Private Corp., Sec. 334e.

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5. EVEN IF THE RULE WERE APPLICABLE IT COULD NOT PREVENT THE STOCKHOLDERS, DIRECTORS AND OFFICERS OF THE ASSOCIATION FROM PARTICIPATING IN THE ELECTION OF TRUSTEE OR EXPRESSING THEIR PREFERENCE, NOR COULD IT BE EXTENDED TO OTHERS SIMPLY BECAUSE THE OTHERS FAVORED THEIR CHOICE OF A TRUSTEE.

The rulings of the referee do not stop at the contention that the election must not be brought about by the officers of the bankrupt. In disapproving

the first election of trustee, Mr. B. G. Tognazzi, he said "that Mr. Tognazzi could not be a candidate again" (p. 21); that the former president of the company, who is "a creditor for all purposes", *must not participate in a general meeting of other stockholder-creditors*, and insisted that they "choose a trustee *without suggestion* of the attorneys, officers or directors of the bankrupt" (p. 22); that they "must choose a disinterested person", (whatever that they may mean where the identity of the creditors is merged in that of the bankrupt) (p. 35); that even "if the majority of the stockholders so desire" they should not have the right to direct that the liquidation be conducted by their officers (p. 43) or by any one suggested by their officers (supra) and directed "that the officers and attorneys *take no part** in the selection of the trustee" (p. 45).

He also excludes all stockholders who think well of their management.

"Mr. Bradford, who was chairman of the meeting at which Mr. Leonard was chosen, testified in effect that he is still of the opinion that Mr. Corbin and Mr. McNab should conduct and lead the liquidation of its concern. While Mr. Bradford is entitled to this view, *he is in my opinion not a proper person to lead the creditors in this matter*, in view of the instructions of the referee that the officers and attorneys of the bankrupt must hold hands off in this election." (p. 36.)

*Italics ours in all cases.

Mr. Bradford was neither an officer nor an attorney, just a stockholder, to be "deemed a creditor for all purposes."

Thus the rule against the activity of the bankrupt, its officers, directors, attorneys and stockholders, has been applied in this case both against officers, directors and attorneys, and also against those of the stockholders whose views agreed with theirs and who supported the same candidate favored by them, but against no others, and, further, the rule has been extended to exclude them also from "taking part in the election" of the trustee or from even "suggesting" the name of a trustee.

Yet even in an ordinary bankruptcy, where the bankrupt and the creditors are not identical and an election in the interest of the bankrupt is not an obvious impossibility, directors, officers and stockholders who are bona fide creditors may take part in the election of trustee and may suggest the trustee.

In re L. W. Day & Co., (C. C. A.) 178 Fed. 545;

In re Ployd, 183 Fed. 791;

In re Syracuse Paper & Pulp Co., 164 Fed. 275;

In re Blue Ridge Packing Co., 125 Fed. 620.

In re Eastlack (*supra*) is a case not unlike the present one, except as to the identity of debtor and creditor. In that case, to quote from the syllabus:

"A debtor stated at a meeting of his creditors that he intended to file a petition in bank-

ruptcy as the best way of liquidating, and that if a person whom he desired could be elected trustee, he thought his estate would pay in full and leave a surplus for himself, and he asked his creditors present to support such person, to which they agreed. After his petition had been filed, a movement having been made by certain creditors to elect a different trustee, and letters having been sent out to creditors in that behalf, a letter was prepared by the bankrupt's attorney which was signed and sent out by a large creditor advocating the election of the bankrupt's candidate. At the creditors' meeting a very large majority of the creditors both in number and in amount of claims voted for such person; so far as appeared without further solicitation on the part of the bankrupt or his attorney, about half of them in number, and three-fourths in amount of claims, being present and voting in person. *Held*, that the facts stated did not justify the referee or court in refusing to approve the election, in the absence of anything showing that it would be detrimental to the interest of any creditor."

The same case is also authority for the proposition that a mere attempt to influence an election is not sufficient unless it has actually had that result.

Id. 74.

In this case as in the Eastlack case, there was not one word of evidence to show that any of the creditors who voted for the majority candidate was actually influenced by any of the acts of the bankrupt's directors and attorneys.

We respectfully submit, therefore, that the referee has not only applied a rule in this case which can have no application under the peculiar facts

of this case, but that he has applied it as against one group of stockholders only, and that he has applied it with a rigor and severity not to be found in any single reported case.

6. THE RULE AGAINST THE ACTIVITY OF THE BANKRUPT IS FOR THE BENEFIT OF THE CREDITORS AND NOT OF THIRD PARTIES.

This requires no argument. Yet a close reading of the certificate will, as we believe, show that the referee has attempted to apply the rule out of consideration for certain state authorities who have absolutely no interest in the administration.

Let us examine the reasons given by the referee for his decision. Why must the rule be applied as he has applied it? Because, he says, building and loan associations "have developed commercially" (p. 43), and "the office of Building and Loan Commissioner is established by law, to examine into the affairs of such concerns" * * * "for the protection of the public dealing with them" (p. 43), and "a fair and impartial administration, including an investigation into the acts of the officers, if such investigation becomes necessary, requires the trustee chosen shall be free from all alliance with the corporation or any of its officers or attorneys, and that the officers and attorneys take no part in the selection of the trustee" (p. 45). It is not quite easy to understand what is meant by the necessity of a "fair and impartial" administration as between creditors and bankrupt

where, as here, they are identical. Nor do we see either reason or logic in requiring the choice of a trustee "free from all alliance with the corporation or any of its officers or attorneys" where the corporation is "in the nature of a corporate co-partnership" and its co-partners are themselves the creditors and the only creditors and have themselves selected their officers and attorneys.

The referee's remarks, therefore, referring as they do to the protection of the public and the duties of the Building and Loan Commissioner in examining into the affairs of such concerns, are eloquent of a confusion of ideas, especially when taken in connection with the fact that no charges of unfairness were made against any of the officers by any of the creditors or any one else, and that the referee embodies in his certificate the complete text of a letter sent by the directors to the stockholders wherein they complained of persecution by certain state authorities.*

*The letter is as follows:

"Dear Sirs: Your Board of Directors enclose herewith, a statement of affairs of your association. Since the attacks, made upon the Association by Building & Loan Commissioner Walker—the righteousness of which attacks was denied by the Courts in judgments adverse to the Commissioner—your Board of Directors deemed it unwise to transact new business, as continual official hostility would have made such course unprofitable to the stockholders.

"Expenses were reduced as far as possible, and every effort was made to expedite liquidation. During this time there has been paid to the stockholders, in the order provided by law, over five hundred thousand dollars. As the assets of the corporation are in long-term mortgages, which cannot be called, and real estate, we consider this excellent progress.

"We call the stockholders' attention to the fact that Commissioner Walker and his accountant stated that the Continental was insolvent, yet since these attacks were made, the Association has paid out over Five Hundred Thousand Dollars, and has assets of more than Eight Hundred Thousand Dollars left, which will, properly administered, pay dollar for dollar to each stockholder."

This letter was introduced, with several others, for the sole purpose of showing the activity of the directors in the election and not for that of showing any unfairness of the management towards any of the stockholders, which was not an issue, and even if it can be considered for any purpose except that for which it was introduced, it shows only, and that by inference, that certain attacks had been made by the state authorities upon the bankrupt association in the courts, wholly outside of this proceeding, and while it was a going concern and subject to the jurisdiction, within legal bounds, of those authorities, and that the attacks were successfully resisted by the association, that they involved charges of insolvency and so injured the business of the association as to make its continuance as a going concern unprofitable. Assuming the truth of these statements, what could be more natural than to seek protection through the liquidation of the company's business in the federal courts, which have so often furnished a harbor of refuge from tyranny and oppression?

This is further emphasized by the fact that the State Superintendent of Banks entered the campaign for trustee. All of these circumstances combine to show a confusion in the mind of the referee and that his ruling, which, we respectfully submit, was not justified upon any theory of protecting the creditors in their statutory right of selection, or of impartiality as between bankrupt and creditor, was in fact based upon some idea of impar-

tiality as between the bankrupt's former managers and those state authorities whose rights of "regulating their conduct" (i. e., the methods of *conducting business* by building and loan associations) "in this state" (p. 43) were, as is evident from the letter in question, the subject of a bitter controversy terminated by the courts adversely to the contentions of the state officials.

It is too obvious for argument that the jurisdiction of the Building and Loan Commissioner does not extend to bankruptcy proceedings; that the necessity of "regulating the conduct" of such associations "for the protection of the public dealing with them" cannot exist when they have ceased to do business; and that a rule devised for the benefit of the creditors cannot be turned against them and that they cannot be made to yield their statutory right of selecting a trustee of their own, either by hunger for power or hope of revenge on the part of state officials who have been balked by the courts from saddling their will upon the bankrupt corporation.

7. THE MERE FACT THAT A PARTIAL LIQUIDATION OF THE AFFAIRS OF A MUTUAL ASSOCIATION WAS EFFECTED BY ITS OFFICERS PRIOR TO THE PETITION IN BANKRUPTCY HAS NO BEARING UPON ANY OF THE QUESTIONS INVOLVED.

The other reason given by the referee for disapproving the election is (p. 45) that "a partial

liquidation has already been had under the direction of" the officers of the bankrupt. No issue of this kind was involved in the hearing, and the writer must frankly admit his inability to see what possible bearing it has upon the right of the majority of the creditors to select a trustee. Moreover, the only proof of the partial liquidation was by way of inference from the letter above discussed, which was introduced by respondents in support of their objection that the association's officers had taken an active part in the selection of the trustee, and it was utterly without any suggestion of irregularity in the partial liquidation.

As to the Trustee's Disqualifications.

The only issues raised in this case were based upon the two objections of counsel for respondents already noted (record p. 23). The one already discussed, that the trustee's election had been brought about by activity on the part of its officers and attorneys; the other (a) that the trustee was the depositary of the bankrupt's deeds of trust, and (b) named as trustee therein.

(a) Not only was the evidence of these supposed disqualifications introduced over the protest of petitioners after they had filed their petition for review, but the points were disregarded by the District Judge, and are clearly not maintainable. For it is not easy to see how the present possession

of deeds of trust by a company elected as trustee, and which would, as trustee, be entitled to them, could disqualify it. To reach such a conclusion we would have to assume at the outset that it was dishonest, a thing which the respondents should be slow to do, since the Anglo-California Trust Company is, like the Union Trust Company, transacting business by the official approval, and under the direction of Mr. Williams, the state official who has placed himself in competition with both of them for the business of acting as trustee, the superintendence whereof has been committed to and undertaken by him in consideration of the annual payment to him of a portion of the taxes levied upon the people of the State.

Moreover, the possession of the deeds of trust is a matter of no consequence whatever since the notes secured thereby carry the security with them, and there is no contention that the notes are in the possession of the trust company.

(b) If the trustee is ineligible because named as such in the deeds of trust, i. e., because given a power of sale in case of delinquency on the part of borrowers, then it follows that there never could be a trustee where the moneys of a bankrupt were secured by mortgages containing a power of sale under Civil Code Sec. 2932.

The complete answer to both of these contentions is, however, that the statute has created no such disability. The only qualifications are com-